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SUBJECT: FINANCE MINISTER SEEKS MORE PARIS CLUB DEBT RELIEF

REF: BELGRADE 1285

¶1. summary: Finance Minister Dinkic has proposed a major Paris Club debt reduction - unrelated to Kosovo - as one element of his so-called "packet plus," a supplement to the GOS action plan for cooperation with the Hague tribunal. This Dinkic initiative proposes bigger, meatier carrots for Serbia, that the international community - according to Dinkic - should provide to speed Serbia's integration into the EU. At the same time, in connection with a revised budget for 2006, Dinkic announced plans to use sizeable privatization revenues to retire World Bank debt, in addition to an already announced pay-off of IMF debt. see action request para 9. end summary

¶2. Finance Minister Dinkic has been touting his "packet plus" for weeks. The stated objective is to accelerate Serbia's development whenever it is finally able to conclude successfully Serbia's cooperation with the International Criminal Tribunal for the Former Yugoslavia. (Dinkic also has pledged to lead a walkout of his G17 party from the GOS if talks with the EU on a Stability and Association Agreement - now on hold based on the lack of ICTY cooperation - do not resume after October 1.) In addition to a further Paris Club debt write-off of some USD 1 billion, Dinkic's packet plus would include easing of visa restrictions by the EU, formal status for Serbia as a candidate for EU accession, and increased EU funding of EUR 250-500 million yearly from 2007-2011 for realization of Dinkic's National Investment Plan.

¶3. (SBU) ECON CHIEF MET WITH VESNA DZINIC, HEAD OF THE FINANCE MINISTRY'S TREASURY DIVISION, ON AUGUST 24 TO SEEK INFORMATION ON SERBIA'S INTENTIONS WITH REGARD TO A FURTHER WRITE-OFF OF PARIS CLUB DEBT. DZINIC CONFIRMED THAT THE GOS WOULD REQUEST A SWAP ON A BILATERAL BASIS FROM THE VARIOUS HOLDERS OF PARIS CLUB DEBT.

¶4. (SBU) DZINIC SAID THAT THE 2001 AGREEMENT BETWEEN SERBIA AND MONTENEGRO AND THE PARIS CLUB PROVIDES FOR THE POSSIBILITY OF SUCH SWAPS. SERBIA WOULD SEEK to carry out such swaps with INDIVIDUAL CREDITOR COUNTRIES and use the proceeds for INFRASTRUCTURE. ITS GOAL IS TO ACHIEVE A total WRITE-OFF OF EURO 850 MILLION (USD 1.09 BILLION) TO BE USED FOR HIGHWAY CONSTRUCTION. (ACCORDING TO A RECENT DINKIC INTERVIEW, MOST OF THE PROCEEDS WOULD BE USED TO COMPLETE CORRIDOR 10 HIGHWAYS TO THE BULGARIAN AND MACEDONIAN BORDERS, ALTHOUGH HE ALSO MENTIONED USING SUCH PROCEEDS FOR ENVIRONMENTAL PROJECTS AND MUNICIPAL INFRASTRUCTURE.) DZINIC SAID THAT GERMANY ALREADY HAD AGREED TO A SMALL SWAP FOR ENVIRONMENTAL PROJECTS.

¶5. While the Ministry of Finance has not made a written request to Embassy for such debt relief, it did make such a request to the Paris Club. Max Hurneus, economic attache at the German Embassy, confirmed on September 12 that Dinkic also had raised the issue with the German ambassador. He said that the Embassy is waiting for an update from the September 13 Paris Club meeting before making any

reply.

16. (SBU) WITH REGARD TO KOSOVO DEBT, DZINIC SAID THAT TECHNICAL TALKS FOCUSED ON RECONCILIATION OF THE DEBT ARE MOVING FORWARD. THE LONDON CLUB HAD NOW PROVIDED SERBIA WITH ORIGINAL DOCUMENTATION, AND THE WORLD BANK IS SENDING DOCUMENTATION ON ITS LOANS. HOWEVER, DZINIC SAID THAT THE PARIS CLUB SECRETARIAT TOLD THE MINISTRY IT MUST OBTAIN SUCH DOCUMENTATION DIRECTLY FROM BILATERAL CREDITORS. DINKIC CONTINUES TO SAY PUBLICLY THAT HE EXPECTS A WRITE-OFF OF SUCH KOSOVO-RELATED DEBT, BUT DZINIC CONFIRMED THAT THERE IS STILL RESISTANCE WITHIN THE GOS BASED ON POLITICAL GROUNDS, I.E., THE BELIEF THAT AGREEING TO A DEBT WRITE-OFF IN SOME WAY WOULD ACKNOWLEDGE A LOSS OF SOVEREIGNTY. DZINIC ASSERTED THAT DINKIC'S SWAP PROPOSAL IS UNRELATED TO THE FATE OF ANY KOSOVO DEBT RELIEF.

17. Dinkic's campaign for debt relief took a new twist when, in connection with an amended 2006 budget approved by the Serbian government on September 7, he announced plans to pay off World Bank debt in 2007. The National Bank of Serbia already has begun to pay off its USD 1 billion debt to the IMF, including a USD 250 million payment in June and another \$250 million by the end of September. Dinkic announced on September 8 that Serbia now plans to pay off its USD 540 million debt to the World Bank in 2007. Dinkic told the press that, altogether, he would like to reduce Serbia's public debt by some USD 2.5-3.5 billion, to less than 35 percent of GDP by the end of the year, thereby transforming Serbia into a country of moderate-to-low indebtedness.

18. (SBU) DZINIC ALSO PROVIDED SOME DETAIL ON PRESS ASSERTIONS THAT GAZPROM HAD ACQUIRED SERBIA'S DEBT TO KUWAIT AND WOULD SOMEHOW USE THIS IN A DEAL INVOLVING A GAS TRANSIT PIPELINE THROUGH SERBIA AND A POSSIBLE MERGER WITH SRBIJAGAS (REFTEL). DZINIC SAID THAT KUWAIT HAD CONSISTENTLY REFUSED TO CONSIDER A WRITEDOWN OF OLD YUGOSLAV DEBT, DESPITE SERBIA'S PARIS CLUB OBLIGATION TO SEEK COMPARABLE TREATMENT FROM OTHER CREDITORS. GAZPROM WAS ARGUING THAT IT COULD ACQUIRE THE DEBT FROM THE KUWAITIS AND THEN PAY IT OFF FROM THE TRANSIT REVENUES SERBIA WOULD RECEIVE FROM A TRANSIT PIPELINE. AT THE SAME TIME, DZINIC COMPLAINED, RUSSIA HAD CONSISTENTLY REFUSED TO PERMIT USE OF SERBIA'S INHERITED CLAIMS ON RUSSIA, BASED ON OLD CLEARING DEBT, TO PAY OFF GAS DEBT. RUSSIA HAD SIGNED A MINUTE AGREEING TO DO SO BUT NEVER FOLLOWED THROUGH, SHE SAID. SHE CONFIRMED THAT SRBIJAGAS IS HAVING A DIFFICULT TIME PAYING ITS CURRENT GAS DEBT TO GAZPROM, ESPECIALLY SINCE ITS PRICES ARE NOT HIGH ENOUGH FOR FULL COST RECOVERY. (IN A SEPARATE CONVERSATION, MILOS TOMIC, THE GENERAL DIRECTOR OF SRBIJAGAS, SAID THAT THE DEBT HAD REACHED USD 250 MILLION.)

19. (U) We would appreciate WASHINGTON GUIDANCE REGARDING PROCEDURES FOR OBTAINING DOCUMENTATION ON U.S. CLAIMS ON SERBIA THAT COULD BE CONSTRUED AS KOSOVO-RELATED DEBT.

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